Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Vargas	Analyst:	Darrine Distefano	Bill Number:	AB 523
Related Bills:	See Legislative History	Telephone:	845-6458	Amended Date:	06-26-2002
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Agency Designate Additional Enterprise Zone in Imperial County

SUMMARY

This bill would require the Technology, Trade, and Commerce Agency (TTCA) to re-designate a manufacturing enhancement area (MEA) within Imperial County into an enterprise zone (EZ).

SUMMARY OF AMENDMENTS

The June 26, 2002, amendments deleted references to the Revenue and Taxation Code relating to sales and use tax on bronchial equipment and inserted the provisions discussed in this analysis.

This is the department's first analysis of this bill.

PURPOSE OF THE BILL

The purpose of the bill is to assist an economically disadvantaged area within Imperial County.

EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative January 1, 2003.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Existing federal law provides special tax incentives for empowerment zones and enterprise communities to provide economic revitalization of distressed urban and rural areas.

Qualified zone businesses operating in federal empowerment zones and federal enterprise communities are eligible to receive two tax incentives: (1) tax-exempt private activity bonds to finance certain facilities; and (2) the "brownfields" tax incentive, which allows taxpayers to expense (rather than capitalize) certain environmental remediation expenditures. Qualified empowerment zone businesses are allowed an additional $20,000 depreciation expense deduction.

Board Position:			Department Director	Date
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Under the Government Code, existing state law provides for the designation of EZs and Manufacturing Enhancement Areas (MEA). Using specified criteria, the TTCA designated two MEAs and 39 of the authorized 42 EZs from the applications received from the governing bodies. EZs are designated for 15 years (except EZs meeting certain criteria may be extended to 20 years), and each MEA is binding for 15 years beginning January 1, 1998.

Under the Revenue and Taxation Code (R&TC), existing state law provides special tax incentives for taxpayers conducting business activities within the EZ. These incentives include sales or use tax credit, hiring credit, business expense deduction, a net interest deduction, special net operating loss treatment, and a tax credit for employees working in an EZ.

Also under the R&TC, existing state law provides a hiring credit as the only incentive for taxpayers conducting business activities within an MEA. The hiring credit is allowable to businesses located in an MEA for a percentage of wages paid to qualified employees. The business may claim up to 50% of the wages paid to a qualified employee as a credit against tax imposed on MEA income. For businesses operating inside and outside an MEA, the amount of hiring credit that may be claimed is limited by the amount of tax on income attributable to the MEA.

THIS BILL

This bill would require TTCA to designate an EZ within Imperial County that was previously designated as an MEA, upon the request of the county's board of supervisors. Once the area has been designated an EZ, the area would cease to exist as an MEA.

This bill also would prevent any new MEA designations after January 1, 2003.

IMPLEMENTATION CONSIDERATIONS

It is unclear what the designation date and expiration date of the designated EZ would be. In the past, when program areas were converted to EZs, the designation date, and thus, the expiration date of the converted program area remained unchanged.

Two MEAs exist in Imperial County (Brawley and Calexico). (However, a portion of Calexico has been designated as an EZ since 1986.) It is unclear whether both MEAs are eligible for designation as an EZ or only one. If both are eligible, it also would be unclear whether the designation would allow for only one EZ to be designated that includes both Calexico and Brawley, or whether two separate EZs would be designated.

This bill would require TTCA to designate either one or both of the MEAs in Imperial County as an EZ, and would provide that the MEA and its benefits would cease on the designation date. Under current law, taxpayers operating in an MEA are eligible to claim a hiring credit. The hiring credit and its carryover are only applied against income and tax generated from activities in the MEA. It is unclear whether the taxpayer would be able to apply the MEA hiring credit and carryover to future years, since the taxpayer would no longer have MEA income.

This bill would state that the benefits obtained in the MEA cease upon designation as an EZ. It is unclear whether a taxpayer would still be allowed to incur new MEA hiring credits or if the taxpayer would lose the right to apply existing MEA hiring credits and credit carryovers obtained in prior tax years.

Once the MEA is designated as an EZ, it is unclear if those employees previously qualifying the taxpayer for the MEA hiring credit would automatically qualify the taxpayer for the EZ hiring credit. If not, the taxpayer would have to obtain new vouchers for those employees.

An MEA has a single tax benefit--the hiring credit. EZs have several different tax benefits (hiring credit, sales and use tax credit, business deduction, net operating loss, and a net interest deduction). It is unclear what impact this bill would have on fiscal year taxpayers that are claiming these tax benefits. Taxpayers that operate on a fiscal year may be in the MEA for the first portion of their taxable year and in an EZ for the remaining portion of their taxable year. It is unclear what tax benefits would be available to the fiscal year taxpayer or how the taxpayer would claim the new benefits.

The conversion of the MEA to an EZ and the treatment of the MEA and EZ tax benefits should be clarified in the MEA and EZ Revenue and Taxation Code provisions. Department staff is available to assist the author's office in drafting the appropriate amendments.

Once the implementation considerations are resolved, implementing this bill would not significantly impact the department's programs and operations.

LEGISLATIVE HISTORY

AB 46 (Washington, Stats. 2000, Ch. 587) expanded the number of EZs from 39 to 42.

AB 499 (Cogdill, 2001/2002) would have required the TTCA to designate a new EZ and TTA within a county within a specified group of counties. This bill was amended June 25, 2002, to instead require General Services to transfer title of a state facility to the City of Norco.

OTHER STATES' INFORMATION

Currently, 29 other states have economic development areas that allow similar tax related incentives to those provided in California's economic development areas. The number of economic development areas varies from state to state. For example, California currently has 53 economic development areas, New York has 58, Florida 32, Illinois 93, and Michigan 23.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in revenue losses as shown in the following table:

Revenue Impact Tax Years Beginning After December 31, 2002 ($ Millions)			
Fiscal Year	2002-03	2003-04	2004-05
	Negligible Loss*	Negligible Loss*	-0.5

Negligible < $250,000.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Revenue Discussion

Total credits used by the Calexico EZ in its third full year were $624,000 in 2000. It was assumed, due to the similarity in geographic and population size to the Calexico EZ, that the proposed EZ in Brawley would use approximately the same amount of credits as Calexico by the 2005-06 fiscal year.

The estimates above allow for the elimination of the current MEA tax benefits for businesses in Brawley and the portion of the Calexico MEA that would qualify as an EZ under this bill.

A similar bill analysis for AB 499 shows a somewhat lower estimate because that revenue analysis was based on 1999 data. The analysis above is based on 2000 data.

LEGISLATIVE STAFF CONTACT

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